

Manufacturing Industrial Council Draft Seattle City Light 2005 Rate Review Presentation

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Key Financial Policies

- Variability Allowance
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Cost Allocation & Rate Design

Seattle City Light Highlights

- From 2000 through 2003 SCL raised rates 4 times for a total of 58%. Cumulatively over that time ratepayers have paid \$546 million more than they would have had rates stayed stable for that time period. They are currently paying \$186 million year more than they paid in 1999.
- The City Council has adopted Financial Policies intended to help restore SCL's financial health. These policies include:
 - Retire short term debt incurred due to the energy crisis of 2000-2002.
 - Set rates so that net revenues available to fund capital requirements will be positive with a probability of 95%.
 - Fund a \$25 million Contingency Reserve.
 - Fund an Operating Cash Reserve of \$30 million.

These Policies were successfully met in 2004 or can be met in 2005. In addition, the Utility's bond outlook from both S&P and Moody's was upgraded.

Seattle City Light Highlights (cont.)

- In its 2005 Annual Report the City Light Advisory Board recommended 2 additional financial policies. These were:
 - Increase the Contingency Reserve to \$100 million.
 - Set an explicit and mandatory target of Debt Capitalization to be 60% by 2011.

These policies have not been adopted.

Utility Rate Benchmarks

Summary of Northwest US Residential and Industrial Rates

Dated February 7, 2005

Residential		% Difference from Most Expensive
Utility	Rate 1,000 Kwh/Month	
National Average (Nov 2004)	\$89.74	9.33%
Portland General	\$82.08	0.00%
Snohomish	\$78.57	-4.28%
Puget Sound	\$74.92	-8.72%
Seattle City Light	\$71.33	-13.10%
PacifiCorp (OR)	\$64.69	-21.19%
Avista (WA)	\$63.70	-22.39%
Tacoma	\$63.07	-23.16%
Idaho Power (ID)	\$61.32	-25.29%
PacifiCorp (WA)	\$57.52	-29.92%
BC Hydro	\$43.20	-47.37%

Regional Average	\$66.04
Seattle City Light % Above/Below Regional Avg.	8.01%

Industrial		% Difference from Most Expensive
Utility	Rate 68% LF, Even Usage	
National Average (Nov 2004)	\$51.21	-6.56%
Seattle City Light	\$54.81	0.00%
Snohomish	\$54.68	-0.24%
Avista (WA)	\$53.80	-1.84%
Puget Sound	\$52.88	-3.52%
Portland General	\$50.42	-8.01%
Tacoma	\$42.86	-21.80%
BC Hydro	\$37.64	-31.33%
PacifiCorp (OR)	\$36.78	-32.90%
PacifiCorp (WA)	\$34.55	-36.96%
Idaho Power (ID)	\$34.05	-37.88%

Regional Average	\$45.25
Seattle City Light % Above/Below Regional Avg.	21.14%

Other Benchmarks

Some Seattle City Light benchmark ratios are within regional parameters:

- Ratepayer served per number of employees.
- Megawatt hours supplied per ratepayer.
- Retail revenues collected per ratepayer.

Summary of Key Accomplishments of City Light since 2001

- Decreased reliance on market purchases and increased reliance on BPA Hydro to serve customer loads. SCL is “long” under all Hydro conditions.
- Retired \$400+ million in short term debt.
- Funded new \$30+ million in operating cash reserve.
- Improved both S&P and Moody’s Bond Outlook.
- Begun funding additional Contingency Reserve in 2005 rates. Funding estimate \$20 million towards goal of \$25 million.
- Reviewing Risk Management practices and how to manage wholesale hydro risk exposure.

Proposed Rate Recommendations

- Because SCL's financial position has improved markedly it is now time for a rate reduction for residential and business ratepayers.
- Retail ratepayers have paid SCL \$545 million since 2000 when compared to rates before the energy crisis.
- Recommendation is to provide a rate reduction in Jan. 2006 of 10% or \$58 million from the retail rate revenue requirement.
- This 10% target will bring SCL rates closer to those of other regional utilities.
- Rate reduction must be balanced with SCL's risk management and "low water" contingency plans.

Financial Policies Summary Table

Issue	Current Proposal	MIC Proposal	Rate Decrease
Variability Allowance	95%	90%	\$20 million
Bond Reserve (cash or insurance product)	Use Insurance	Use Insurance	NA
Contingency Reserve	\$130 million	\$55 million	NA
Debt/cap ratio target 2011	60% Target	60% Target	NA

See details in Appendix 1.

Revenue Requirement Cost Reduction Targets

- Existing 2006 Rate proposal proposes \$ 575 million retail revenues collected:
 - Purchased Power – 287 million.
 - Operating Expense & Tax payments - \$211 million.
 - Debt Service - \$137 million.
 - Revenue “credits” – 60 million.

Revenue Requirement Cost Reduction Targets (cont.)

- Revenue Requirement rate savings opportunities to target:
 - Capital budget forecasts.
 - Target cost reductions of 2-4% in 2006 \$211 million operating budget. Equals \$4-\$8 million year.
 - Bond Reserve savings can contribute
 - Cost reduction opportunities in power purchase costs should be investigated.
 - Seek cost savings within 2005 activities identified in City Council work plan and from Advisory Board Annual Report. These include:
 - City Council Work Plan – Capital spending and reliability indices.
 - Advisory Board - Transfers from SCL funds to General Fund.

Cost Allocation & Rate Design

- Retail rates indicate costs are disproportionately loaded more heavily on commercial and industrial customers when compared to peer utilities.
- Consultants are collecting data from SCL staff.
- Reviewing cost allocation and rate design principles of peer utilities including Puget, PacifiCorp and others. Review alternative rate options.
- Will have recommendations by April.

Summary – proposal is balanced

- Provides ratepayers some relief.
- Fund rate reductions first out of net operating revenues.
- “Long” power supply position eliminates risk SCL will be short supply.
- Cash contingency fund of \$25 million, \$30 million operating cash reserve and cash available from bond reserve supports capital ratio targets.
- New SCL power supply management team in place to manage wholesale revenue risk.

Appendix 1

Recommendation on Variability Allowance

- Modify Variability Allowance
- For example 90% factor results in revenue requirement decrease in 2006 of 20 million.
- When coupled with \$30 Million & \$25 million contingency reserves and new risk management emphasis and team - future SCL financial risks are adequately covered.
- Variability allowance target must be linked with cash reserves.
- Consider coupling with rate adjustment mechanism.

Recommendation on Bond Reserve or Insurance Product

- Use part of Bond Reserve to fund Contingency Reserve.
- SCL currently has about \$85 million cash in a bond fund reserve account.
- The bond reserve can be replaced with a Surety bond without jeopardizing bond covenants.
- Recommendation is to use bond reserve to partially fund “low water” contingency reserve.

Recommendations on Contingency Reserves

- Operating Cash Reserve - Retain \$30 million Operating Cash Balance adopted in 2001. Actual balance 11/04 = \$43 million (Moody's).
- “Low Water Year” Contingency Reserve - Target \$25 million for Contingency Reserve.
- 2006 net wholesale revenue forecast is \$133 Million. Actual average net wholesale revenues 2002 – 2004 = \$106 million. \$133 minus 105 = 25 million year at “risk”. \$25 million cash contingency allows 1 year of coverage.
- Retain \$20 million being collected in 2005 rates to initially fund Contingency Reserve rather than returning this money to ratepayers.
- Supplement \$20 million being collected in rates with cash from Bond Reserve to meet \$25 million target.

Recommendation on Target Debt/Cap Ratio

- Retain existing targets proposed by Mayor & Advisory Board but fund 10% rate reduction first.
- Rate reduction will impact amount of net operating cash to fund capital program. If any “shortfall” occurs options are - defer capital expenditures, cut additional expenses, consider rate adjustment mechanism or increase percent of debt to fund critical capital needs.
- Impact in 2006 incremental debt capital structure changes from 23% of total capital needs to 36%.